

The transfer of special order printing materials is a service transaction that may result in either Service Occupation Tax or Use Tax liability for the servicemen, depending upon which tax base the servicemen choose to calculate their liability. See 86 Ill. Code 140.101 through 140.109. (This is a GIL.)

November 29, 2004

Dear Xxxxx:

This letter is in response to your letter dated March 1, 2004, in which you request information. The Department issues two types of letter rulings. Private Letter Rulings ("PLRs") are issued by the Department in response to specific taxpayer inquiries concerning the application of a tax statute or rule to a particular fact situation. A PLR is binding on the Department, but only as to the taxpayer who is the subject of the request for ruling and only to the extent the facts recited in the PLR are correct and complete. Persons seeking PLRs must comply with the procedures for PLRs found in the Department's regulations at 2 Ill. Adm. Code 1200.110. The purpose of a General Information Letter ("GIL") is to direct taxpayers to Department regulations or other sources of information regarding the topic about which they have inquired. A GIL is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120. You may access our website at www.ILTAX.com to review regulations, letter rulings and other types of information relevant to your inquiry.

The nature of your inquiry and the information you have provided require that we respond with a GIL. In your letter you have stated and made inquiry as follows:

Please be advised that ABC represents a corporation (hereinafter, the 'Company') that requests a tax ruling regarding its business activities in Illinois. Accordingly, we respectfully request that the Illinois Department of Revenue (hereinafter, the 'Department') issue a tax ruling regarding the application of the Illinois Retailer's Occupation Tax, Use Tax, Service Occupation Tax, and Service Use Tax to the Company's business activities in Illinois as described below. However, due to confidentiality reasons, we are unable, at this stage, to disclose the name of the company for which we act.

I. Facts

The Company is a marketing services firm that supports federal, state, and local governments. The Company does this by forming public-private partnerships with government agencies to provide on-line and off-line products and services at the moment consumers need them, using advertising to cover all government costs, generate revenue, and save consumers time and money.

The Company provides two principal products in Illinois. For these two products the Company partners with the United States Government to prepare certain government issued documents and forms for distribution to the general public. Specifically, the Company and the federal government have contractually entered into a strategic alliance. (Provisions included in the strategic alliance agreement that relate to the establishment of a 'strategic partnership' and 'agency relationship' between the Company and the federal government are included in the attached Addendum.) The Company is the only entity authorized by the federal government to print these particular forms.

On behalf of the federal government, the Company prepares the aforementioned documents and forms and pairs them with promotional and advertising materials from third party vendors. For purposes of this discussion, we will refer to this combination of materials as the 'Federal Government Package.' The Federal Government Package is an official government mailing, i.e., the mailing envelope bears the government agency's official logo, the government agency's return address, and an official postage permit indicia.

Preparation of the Federal Government Package occurs as follows:

- Upon request and approval of the federal government, the Company enters into an agreement with a third party printer¹ to print documents and forms on behalf of the federal government.
- At or about the same time, the Company contracts with private business enterprises that seek to advertise their goods and/or services to a specific consumer base. Once the Company enters into an agreement with a client, the Company prepares a draft layout of an advertisement (subject to client approval) to be included in the package. The Company then hires a third-party printer² to print the advertising materials on behalf of the client.
- Once the printed materials have been produced, a subcontractor bindery/mailing house binds the printed materials together (i.e., the packages). The Federal Government Package is then delivered to either the federal government office in Illinois or directly to an individual's residential address in Illinois.

The Company provides its service at no cost to the federal government and at no cost to the recipients of the Package. Under the terms of the contract, the federal government has the potential to receive a portion of the advertising revenue.

The Company generates revenue in part from the delivery of packages to Illinois addresses. Specifically, the Company's revenue is derived from advertising fees associated with the Federal Government Package. The Federal Government Package is sent from the third party bindery/mailing house to: (i) the requesting government office for on-site distribution; (ii) directly to a predetermined residential address as directed by the federal government supplied mailing list; or (iii) to a specific customer address upon request.

II. Question Presented

Does Illinois Retailer's Occupation Tax, Use Tax, Service Occupation Tax, or Service Use Tax apply to the Company's printed materials, including the advertising materials and/or the government documents delivered inside Illinois?

III. Ruling Requested

The Company's printed materials are exempt from Illinois Retailer's Occupation Tax, Use Tax, Service Occupation Tax, or Service Use Tax for at least one or more of the following reasons: (1) the transaction is not considered a 'sale' for either Illinois Retailer's Occupation Tax or Use Tax purposes; (2) the sale is exempt as a sale to the federal government; and/or (3) the transaction is a non-taxable service transaction and any purchases that are made by the service provider are made on behalf of and as an agent for the federal government.

IV. Analysis

Please note that the Company has never collected Illinois Retailer's Occupation Tax or Service Occupation Tax. In fact, the Company believes that it is not subject to the Retailer's Occupation Tax, Use Tax, Service Occupation Tax, or Service Use Tax in the state.

In Illinois, unless an exemption applies, a tax (the Retailer's Occupation Tax) is imposed upon persons in the business of selling tangible personal property at retail. 35 Ill. Comp. Stat. 120/2. The term 'sale at retail' is defined as any transfer, except for resale, of the ownership of or title to tangible personal property to a purchaser for a valuable consideration. 35 Ill. Comp. Stat. 120/1. However, sales of personal property to any governmental body are specifically exempted from Illinois Retailer's Occupation Taxes. 35 Ill. Comp. Stat. 120/2-5(11).

In addition to the Retailer's Occupation Tax, Illinois imposes a tax (the Use Tax) upon the privilege of using in the state tangible personal property purchased anywhere at retail from a retailer. 35 Ill. Comp. Stat. 105/3. This tax does not apply if the seller of the tangible personal property would not be subject to tax in Illinois if the sale had occurred in Illinois. 35 Ill. Comp. Stat. 105/3-5. Furthermore, purchases of personal property by a governmental body are specifically exempt from the Illinois Use Tax. 35 Ill. Comp. Stat. 105/3-5.

Lastly, Illinois imposes a tax (the Service Occupation Tax/Service Use Tax) upon the privilege of using in Illinois real or tangible personal property acquired as an incident to the purchase of a service from a serviceman. 35 Ill. Comp. Stat. 110/3. However, a 'sale of service' means any transaction except (i) one that is subject to the Retailer's Occupation Tax or Use Tax or (ii) a sale or transfer of tangible personal property as an incident to the rendering of service for or by any governmental body. 35 Ill. Comp. Stat. 115/2.

The Company believes that its business activities in the State of Illinois are not subject to the Retailer's Occupation Tax, Use Tax, Service Occupation Tax, or Service Use Tax in the state. The Company offers the following in support of its position:

- For Illinois Retailer's Occupation Tax and Use Tax purposes, the term 'sale at retail' is defined as any transfer, except for resale, of the ownership of or title to tangible personal property for a valuable consideration. See 35 Ill. Comp. Stat.

120/1 and 105/2. In the instant case, the Company provides the package to the federal government and the residents of Illinois at no cost and the Company does not receive consideration from the federal government or the residents of Illinois in return for the tangible personal property (i.e., the packages). Since consideration is required to consummate an Illinois retail sale, the Company takes the position that the transaction is not a retail sale for Illinois Retailer's Occupation Tax and Use Tax purposes.

- If the Department is of the opinion that the Company's transfer of the package is considered a retail sale for Illinois Retailer's Occupation Tax and Use Tax purposes, the Company takes the position that the sale is exempt from Illinois Retailer's Occupation Tax and Use Tax as a sale to the federal government. See 35 Ill. Comp. Stat. 120/2-5(11) and 105/3-5.
- In the alternative, the Company takes the position that it is providing a service and is not selling tangible personal property in Illinois and any purchases made by the Company were made on behalf of and as an agent for the federal government. As a service provider, we understand that the Company may be taxable under the Service Use Tax on the cost of materials used in performing its services (i.e., costs associated with paper and printing). However, we believe that the costs of producing the Company's products are not subject to Illinois Service Use Tax because the transaction would not be subject to the Service Occupation Tax since the service is being provided to a governmental body (i.e., the Federal Government). See 35 Ill. Comp. Stat. 115/2. Furthermore, the Company has been given agency powers by the federal government with respect to certain activities. Purchases made by an agent on behalf of the federal government would be exempt from the Illinois Retailer's Occupation Tax and Use Tax. See 35 Ill. Comp. Stat. 120/2-5(11) and 105/3-5.

If it is the Department's position that additional facts are needed to make a determination as to whether the Company has Illinois Retailer's Occupation Tax, Use Tax, Service Occupation Tax, or Service Use Tax liability, we can provide more specific facts as to the Company's activities and relationship with the federal government.

The Company would appreciate a tax ruling at your earliest convenience. If you have any questions or would like to discuss the matter further, please do not hesitate to call me.

DEPARTMENT'S RESPONSE:

Without reviewing the Company's specific contractual obligations with the government and third party vendors, and without the registration status of the servicemen involved, the Department is without sufficient information to provide you with a specific response. However, I hope the following information regarding Service Occupation Tax and Service Use Tax are helpful.

If an alliance with a governmental agency is formed wherein a company is providing tangible personal property to the governmental agency free-of-charge, then a donor/donee situation may exist. A donor who purchases tangible personal property and gives the tangible personal property to a donee makes a taxable use of the property when making the gift. See 86 Ill. Adm. Code 150.305(c). A donor owes Use Tax on the donor's cost price of the tangible personal property that is transferred.

The Service Occupation Tax is a tax imposed upon servicemen engaged in the business of making sales of service in this State, based on the tangible personal property transferred incident to sales of service. See 35 ILCS 115/3.

Under Illinois tax law, the transfer of special order printing materials is a service transaction that may result in either Service Occupation Tax or Use Tax liability for the servicemen, depending upon which tax base the servicemen choose to calculate their liability. For general information, see 86 Ill. Code 140.101 through 140.109 regarding sales of service and Service Occupation Tax.

A serviceman's liability may be calculated in one of four ways: 1. Separately stated selling price of tangible personal property transferred incident to service; 2. 50% of the serviceman's entire bill; 3. Service Occupation Tax on the serviceman's cost price if he is a registered de minimis serviceman; or, 4. Use Tax on the serviceman's cost price if he is a de minimis serviceman not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act.

Using the first method, servicemen may separately state the selling price of each item transferred as a result of the sale price of service. The tax is then calculated on the separately stated selling price of the tangible personal property transferred. If the servicemen do not separately state the selling price of the tangible personal property transferred, they must use 50% of the entire bill to the service customer as the tax base. Both of the above methods provide that in no event may the tax base be less than the serviceman's cost price of the tangible personal property transferred. See 86 Ill. Adm. Code 140.106. These methods result in the customer incurring a Service Use Tax liability. See 86 Ill. Adm. Code 160.101.

The third way servicemen may account for their tax liability only applies to de minimis servicemen who have either chosen to be registered or are required to be registered because they incur Retailers' Occupation Tax liability with respect to a portion of their business. See 86 Ill. Adm. Code 140.109. Servicemen may qualify as de minimis if they determine that the annual aggregate cost price of tangible personal property transferred incident to the sale of service is less than 35% of the total annual gross receipts from service transactions (75% in the case of pharmacists and persons engaged in graphics arts production). Servicemen no longer have the option of determining whether they are de minimis using a transaction by transaction basis. Registered de minimis servicemen are authorized to pay Service Occupation Tax (which includes local taxes) based upon their cost price of tangible personal property transferred incident to the sale of service. Such servicemen should give suppliers resale certificates and remit Service Occupation Tax using the Service Occupation Tax rates for their locations. This method also results in the customer incurring a Service Use Tax liability.

The final method of determining tax liability may be used by de minimis servicemen that are not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act. Such de minimis servicemen handle their tax liability by paying Use Tax to their suppliers. If their suppliers are not registered to collect and remit tax, the servicemen must register, self-assess and remit Use Tax to the Department. The servicemen are considered to be the end-users of the tangible personal property transferred incident to service. Consequently, they are not authorized to collect a "tax" from the service customers. See 86 Ill. Adm. Code 140.108. Under this method the customer incurs no Service Tax liability.

If your client is taking orders for personalized business forms and then farms these orders out to special order printers who actually do the work, then your client is functioning as a primary serviceman in a multi-service situation. The taxability of a primary serviceman in a multi-service situation is set out in 86 Ill. Adm. Code 140.145.

I hope this information is helpful. If you require additional information, please visit our website at www.ILTAX.com or contact the Department's Taxpayer Information Division at (217) 782-3336. If you are not under audit and you wish to obtain a binding PLR regarding your factual situation, please submit a request conforming to the requirements of 2 Ill. Adm. Code 1200.110 (b).

Very truly yours,

Edwin E. Boggess
Associate Counsel

EEB:msk

¹ Although the Company contracts with third-party printers in Illinois and STATE to print both the government documents and the advertising supplements, the majority of these items are shipped outside these states.

² See footnote 2.